United Nations E/2004/18

Economic and Social Council

Distr.: General
7 April 2004

Original: English

Substantive session
28 June-30 July 2004
Item 10 of the provisional agenda*
Regional cooperation

Summary of the economic and social survey of Asia and the Pacific, 2004

Summary

Developing countries in the Economic and Social Commission for Asia and the Pacific (ESCAP) experienced strong, broad-based growth in 2003 combined with low inflation. ESCAP developing countries as a group are growing faster than the global economy as well as other groups of developing countries. Growth is becoming more autonomous, driven increasingly by forces within the region, such as intraregional trade and strong domestic demand, with China's economy playing a major role in the former. Growth in the developed countries was above expectations, as Japan's economy recovered strongly in 2003. Prospects for 2004 indicate a continuation of existing trends on the assumption that the region experiences no negative shocks, the unravelling of global imbalances does not generate major disruptions in the financial markets and the economies of the region are able to maintain sound macroeconomic fundamentals, while implementing ongoing programmes of reform and sustaining competitiveness at the same time.

Despite the region's robust economic growth and significant strides in poverty reduction over the past several decades, poverty continues to be a major development challenge for many countries in the region. The complexity and multidimensional nature of poverty make tackling it a difficult task. That is where well-designed national strategies for poverty reduction, supported by appropriate institutions and political will, make a difference. Some countries have their own national poverty reduction strategies while others have adopted the Poverty Reduction Strategy Paper (PRSP) approach to focus attention on measures to tackle poverty. A study of 13 countries which have adopted the PRSP approach shows that it could well be an

* E/2004/100.

04-30184 (E) 260504

effective tool for poverty reduction if it is aligned explicitly with the Millennium Development Goals. There should be better analysis of the root causes of poverty, fuller consideration of the downside risks of internal and external shocks and more integration with budgetary and parliamentary processes. As a major stakeholder in the global efforts to reduce poverty, the international community can play a critical role in facilitating national efforts.

The present document is based on the *Economic and Social Survey of Asia and the Pacific 2004*.

Contents

		Page
I.	Implications of recent economic and social developments	3
II.	Policy issues and challenges	9
III.	Poverty reduction strategies: tackling the multidimensional nature of poverty	12

I. Implications of recent economic and social developments

1. The *Economic and Social Survey of Asia and the Pacific 2004* looks at trends in the regional economy in 2003, prospects for 2004 and the policy choices facing the region. It also considers longer-term issues relating to poverty reduction strategies in the region in the light of the multidimensional nature of poverty.

2. The *Survey* states that in 2003 the developing countries in the region of the Economic and Social Commission for Asia and the Pacific (ESCAP) continued to show strong growth, exceeding the 2002 performance by almost half a percentage point. The performance in 2002 itself had significantly exceeded expectations so that by the end of 2003, following the 2001 slowdown, ESCAP developing countries had enjoyed two years of buoyant growth combined with low inflation. From a regional perspective, growth was broad-based, with all subregions but one experiencing higher growth and was not affected significantly by the war in Iraq and the severe acute respiratory syndrome (SARS) crisis. The experience with inflation was mixed, with two subregions having somewhat higher inflation in 2003 compared with 2002, albeit at a low absolute level, with the exception of some of the Pacific island economies (see table 1).

3. Buoyant growth in the ESCAP developing countries note only represents an impressive turnaround after the 2001 slowdown, but also shows that the process is becoming less dependent upon global economic trends. ESCAP developing countries as a group are growing faster than both the global economy and other groups of developing countries. As such, growth is becoming more autonomous in that it is the result primarily of forces within the region, such as intraregional trade and strong domestic demand, although exports to the rest of the world continue to play a significant part in sustaining the overall momentum of growth.

4. China's remarkable performance has been central in sustaining the momentum of growth in the region as a whole, with its gross domestic product (GDP) expanding by just under a quarter in only three years (2001-2003) on the basis of strong investment and consumption demand. During this period, China also increased total imports by more than $160 billion, some two thirds of which have come from the region. China is now the fourth-largest trading nation in the world, helping thus to stimulate output growth across a broad front in the regional economy. Similar trends are visible in several other economies of the region, where robust growth has resulted from a combination of higher net exports and domestic demand. The former is the result partly of higher commodity prices and partly of higher growth of information and communication technology components plus a wide range of finished consumer goods, especially household electronics. Higher exports have also been the result of strong demand from within the region and have been further boosted by stronger growth in the United States of America, to which approximately a fifth of the region's exports remain destined. Robust domestic demand owes much to higher fiscal spending as well as to increased corporate and household expenditure, which has been facilitated by the low-inflation and low-interest rate environment.

Table 1
Selected economies of the ESCAP region: rates of economic growth and inflation, 2002-2006
(Percentage)

	Real GDP					*Inflation*[a]				
	2002[b]	*2003*[c]	*2004*[c]	*2005*[c]	*2006*[c]	*2002*[b]	*2003*[c]	*2004*[c]	*2005*[c]	*2006*[c]
Developing economies of the ESCAP region[d]	5.7	6.0	6.2	6.0	6.0	5.5	3.6	3.0	2.7	2.3
South and South-West Asia[e]	5.2	6.6	5.8	6.3	6.4	14.4	10.6	7.9	6.5	5.0
Bangladesh	4.4	5.3	5.7	6.0	6.5	2.4	5.1	4.5	4.0	4.0
Bhutan	7.7	7.0	7.5	8.0	9.0	2.7	3.6	..	..	..
India	4.3	7.5	6.0	6.6	6.7	4.0	4.8	4.0	3.5	3.0
Iran (Islamic Republic of)	6.5	6.9	7.1	8.1	8.2	15.8	16.8	17.0	16.0	13.0
Nepal	-0.6	2.4	3.5	4.5	..	2.9	5.0	4.8	..	..
Pakistan	3.4	5.1	5.3	5.8	6.0	3.5	3.1	4.0	4.0	4.0
Sri Lanka	4.0	5.5	6.0	6.5	7.0	9.6	6.3	6.0	5.5	5.0
Turkey	7.8	5.3	5.1	5.1	5.1	45.0	25.3	14.4	9.8	6.2
South-East Asia	4.2	4.5	5.8	5.7	5.8	4.6	3.3	3.7	3.7	3.1
Cambodia	5.5	5.0	5.6	5.5	..	3.4	1.7	4.3	5.0	..
Indonesia	3.7	4.1	4.8	4.4	4.5	11.9	6.6	6.2	6.0	4.1
Lao People's Democratic Republic	5.9	5.9	6.1	6.0	6.3	10.6	13.5	9.0	5.0	5.0
Malaysia	4.1	5.2	5.5	6.0	5.5	1.8	1.2	1.8	2.2	2.0
Myanmar	5.3	5.1	4.3	..	..	57.1	52.8	44.0	40.0	..
Philippines	4.4	4.5	5.4	5.8	6.3	3.1	3.1	4.5	4.0	3.5
Singapore	2.2	1.1	4.7	4.4	4.9	-0.4	0.5	1.1	1.5	1.9
Thailand	5.4	6.3	8.0	7.5	7.5	0.7	1.8	2.4	2.5	2.8
Viet Nam	7.0	7.2	7.5	8.0	8.0	3.9	3.0	4.3	4.8	4.9
East and North-East Asia	6.4	6.0	6.6	6.1	6.2	0.1	1.4	1.3	1.2	1.2
China	8.0	9.1	8.5	8.0	7.8	-0.8	1.2	1.0	0.8	0.5
Hong Kong, China	2.3	3.0	5.1	4.0	3.4	-3.1	-2.6	-0.5	0.3	1.0
Mongolia	4.0	5.0	5.3	5.5	5.5	1.5	5.0	5.0	5.0	5.0
Republic of Korea	6.3	3.0	4.5	4.2	5.0	2.7	3.6	2.7	2.4	2.5
Taiwan Province of China	3.6	3.3	5.4	4.9	4.7	-0.2	-0.3	0.4	0.9	1.0
North and Central Asia	5.4	7.7	5.1	4.6	4.2	14.3	11.5	10.6	8.8	8.1
Armenia	12.9	13.9	7.7	7.5	..	1.0	4.7	3.3	4.0	..
Azerbaijan	10.6	11.2	8.7	12.0	..	2.8	2.2	3.0	3.6	..
Georgia	5.6	8.6	6.5	12.0	..	5.7	4.8	5.2	6.0	..
Kazakhstan	9.8	9.2[f]	8.3	9.5	6.5	6.0	6.4	6.4	6.4	6.0
Kyrgyzstan	-0.5	6.7	4.4	5.5	..	2.1	3.1	3.5	3.6	..
Russian Federation[g]	4.7	7.3	4.8	4.1	4.1	15.1	12.0	11.1	9.0	8.2
Tajikistan	9.5	10.2	6.0	6.0	..	10.2	17.1	15.0	10.0	..

	Real GDP					Inflation[a]				
	2002[b]	2003[c]	2004[c]	2005[c]	2006[c]	2002[b]	2003[c]	2004[c]	2005[c]	2006[c]
Turkmenistan	21.2	23.1	9.8	10.0	..	10.6	10.5	11.5	12.0	..
Uzbekistan	4.2	4.4	3.0	3.0	..	24.2	13.9	10.0	11.0	..
Pacific island economies	0.5	2.8	3.1	2.2	2.5	8.4	12.7	7.9	..	..
Cook Islands	2.2	1.8	0.2	..	..	3.9	2.4	1.8	..	..
Fiji	4.1	5.0	4.1	3.5	3.6	0.8	3.8	3.0[b]	..	..
Papua New Guinea	-0.8	2.0	2.8	1.7	2.1	11.8	17.5	10.1	11.8	..
Samoa	1.8	3.5	3.5	..	..	8.1	4.1	2.8	..	..
Solomon Islands	-2.0	1.9	3.1	..	..	9.8	12.1	11.0	..	..
Tonga	1.6	2.0	2.6	..	..	10.3	10.5	13.8	..	..
Vanuatu	-2.8	1.0	2.0	2.6	2.8	2.2	2.5	2.9	..	..
Developed economies of the ESCAP region	-0.1	2.7	2.2	1.6	1.1	-0.6	-0.1	0.0	-0.05	-0.05
Australia	3.6	2.8	3.6	3.7	3.7	3.0	2.7	2.3	2.7	2.5
Japan	-0.4	2.7	2.1	1.4	0.9	-0.9	-0.3	-0.2	-0.3	-0.2
New Zealand	4.2	2.7	3.1	3.1	3.2	2.6	1.7	2.2	2.4	2.3

Sources: ESCAP, based on national sources; International Monetary Fund, *International Financial Statistics*, vol. LVI, No. 12 (December 2003); Asian Development Bank, *Key Indicators of Developing Asian and Pacific Countries 2003* (Asian Development Bank, 2003) and *Asian Development Outlook 2003 Update* (Asian Development Bank, 2003); Economist Intelligence Unit, *Country Reports* and *Country Forecasts* (London, 2003 and 2004), various issues; and web site of the Interstate Statistical Committee of the Commonwealth of Independent States, www.cisstat.com, 4 February 2004.

Note: Data correct as at 4 March 2004.

[a] Changes in the consumer price index.

[b] Estimate.

[c] Forecast/target.

[d] Based on data for 38 developing economies representing more than 95 per cent of the population of the region (including the Central Asian republics); GDP figures at market prices in United States dollars in 2000 (at 1995 prices) have been used as weights to calculate the regional and subregional growth rates.

[e] The estimates and forecasts for countries relate to fiscal years defined as follows: fiscal year 2003/04 = 2003 for India, the Islamic Republic of Iran and Myanmar; and fiscal year 2002/03 = 2003 for Bangladesh, Nepal and Pakistan.

[f] January-November.

[g] In case of inflation, figures for 2002-2003 refer to year-end rates.

[h] Year-end figure.

5. Although the prospects for each subregion are different, broadly speaking, the trends outlined above are expected to continue over the next 12 months in the ESCAP region as a whole; this is subject to the caveat that there are no new negative shocks to the region's economy in 2004. The expectation is that, barring any significant negative shocks, the collective GDP growth rate in the ESCAP developing countries should be the same in 2004.

6. In this context, it is worth noting that at the time of writing, avian influenza had affected 10 economies in the region, mainly in East and South-East Asia, resulting in the culling of millions of chickens on poultry farms across the region and in a number of deaths of human beings. The future course of this problem, particularly its wider economic repercussions in the region, is difficult to predict with precision for the time being. However, assuming that the disease remains

confined to poultry farms and is contained, say, by the end of April, its impact on regional growth is likely to be negligible and could even be made up by faster growth in the second half of the year, as happened with SARS in 2003.

7. Nevertheless, this optimistic scenario should be qualified with risks that could operate on the downside. In the first place, from a global standpoint, the latter part of 2003 witnessed the emergence of major global imbalances. The unravelling of those imbalances, especially in the form of rapid fluctuations in exchange rate parities, could spill over into greater instability in the financial markets, thereby undermining business and consumer confidence alike. Second, the danger of protectionist tendencies cannot be ruled out, given the implicit changes in relative competitiveness via exchange rate changes superimposed upon the failure of the World Trade Organization negotiations at Cancún, Mexico, in September 2003. Third, the stimulation of domestic demand by higher fiscal spending and low interest rates for three years or more has raised both public debt and personal indebtedness to uncomfortably high levels in a number of economies. Many of them thus do not have significant additional scope to stimulate growth further by these means. Fiscal consolidation and some degree of monetary tightening may soon become unavoidable. The following paragraphs outline briefly the performance and prospects for each subregion, followed by a discussion of the principal policy issues facing the region in the near term.

8. In East and North-East Asia, the rapid growth of the Chinese economy was not able to offset fully the marked slowdown in the Republic of Korea and weaker growth in Taiwan Province of China. Hence, it was the only subregion to experience a slowdown in the overall GDP growth rate in 2003 compared with 2002. Inflation rose, but at 1.4 per cent it remains low by historical standards and lower than in the other developing economies of the region. Prospects for 2004 are for a modest acceleration in the collective growth rate even though China's economy is expected to slow marginally from its present high rate of expansion. Thus, the pickup in regional growth will be on account of the higher momentum of development in the other economies of the subregion.

9. Despite the robust GDP growth, persisting and rising fiscal deficits are the central near-term policy issue of concern in the subregion. Domestic saving rates are high and financing these deficits does not pose an immediate problem. However, the effective pre-emption of resources on a large scale by the Governments of the subregion reduces the policy space to address urgent problems in the financial sector, as, for instance, in China, or to promote structural change and improve competitiveness, as, for instance, in Hong Kong, China, and the Republic of Korea. Moreover, the accumulating public debt is almost certainly bound to create upward pressure on interest rates in due course, thus putting at risk long-term investment expenditure in the various economies. Some restructuring and reform of the fiscal system are needed to stabilize the public debt-to-GDP ratio over the medium term. Furthermore, a shift from indirect to direct taxes is needed on equity grounds.

10. Collective GDP growth in North and Central Asia accelerated by an impressive 2.5 percentage points in 2003. The already high rates of growth prevailing in the smaller economies, such as Armenia, Azerbaijan, Georgia, Tajikistan and Turkmenistan, went up further in 2003; Kazakhstan continued to make progress in developing its energy resources and maintained its robust growth of recent years; Kyrgyzstan emerged smartly from negative growth; and Uzbekistan improved upon

its somewhat modest 2002 growth rate. The economy of the Russian Federation exceeded all expectations by achieving growth considerably in excess of the rate predicted as recently as six months ago and 2.6 percentage points more than in 2002. This stellar performance was driven by the traditionally strong energy and other natural resource sectors, aided by the continued diversification of the economy. Overall industrial production stood nearly 8 per cent higher in December 2003 on a year-on-year basis. Prospects for 2004, however, suggest that current rates of growth are unlikely to be sustained, with all economies expected to experience some slackening in the pace of growth in the coming months as energy and commodity prices soften.

11. This subregion's economies in transition face a very different set of qualitative issues of day-to-day management and of long-term development compared with the other ESCAP subregion. Transition from the command economy to a market-based one is taking longer than initially perceived. Deregulation of the price system is still incomplete and progress in reducing the role of the Government in production and distribution has some way to go. Deregulation of the price system is needed to eliminate repressed price pressures and achieve and maintain longer-term macroeconomic stability. Meanwhile, improved policy transmission is predicated on a reduction in the role of the Government and the establishment of stronger oversight institutions accompanied by the wider application of market-sensitive prices and instruments. Progress is being made on both fronts, as can be seen in the declining rates of inflation, lower fiscal deficits and improved current account positions in all except three countries in North and Central Asia. This progress is providing greater stability in exchange rates and a more stable environment for investment, both domestic and foreign. However, institutional progress has been slower and more uneven, especially in the financial sector, a key interface between the real economy and the saving and investment decisions of individuals. Market signals tend to operate poorly in capital allocation decisions, leading to waste and inefficiency.

12. The Pacific island economies emerged from two years of recession in 2003 as higher agricultural commodity prices stimulated output growth in the subregion. At the same time, however, inflationary pressures intensified, especially in the larger economies of Papua New Guinea and Fiji, on account of higher energy prices feeding into higher production and transport costs. Prospects for 2004 suggest an easing of both GDP growth and price pressures.

13. Several economies are running fiscal deficits and remain dependent upon outside assistance for budgetary support, a phenomenon that remains a key area of concern in this part of the world. The existence of inefficient State-owned firms and poor governance aggravates the fiscal problem significantly, while the shortage of public resources has meant chronic underinvestment in physical infrastructure, especially communications, a critical necessity given the physical remoteness and vulnerability to natural disasters of the island economies. The aggregate impact of these shortcomings has led to an increase in poverty and growing social instability in several parts of this subregion. Substantial and sustained investment in physical infrastructure and in education and health facilities is vitally needed to improve economic performance and the quality of life of the citizens of the Pacific island countries in the coming years.

14. In South and South-West Asia, there was a marked improvement in the collective GDP growth rate in 2003, compared with 2002, along with the abatement of inflationary pressures over much of the subregion. The higher GDP growth was almost exclusively accounted for by India, the largest economy in the subregion, which improved its GDP growth rate by over 3 percentage points. Pakistan, Bangladesh and Sri Lanka also experienced better GDP growth rates to varying degrees. The smaller economies likewise did well, with Nepal emerging from negative growth in 2002. The improved growth performance in India and Pakistan was occasioned by more favourable weather, which aided strong output growth in agriculture. Exports also benefited, particularly in Pakistan. Higher output and better commodity prices raised agricultural incomes and this, in turn, stimulated the production of manufactured goods. Investment levels also went up in these two economies. Elsewhere, the Islamic Republic of Iran too improved on its 2002 performance on the basis of strong demand and continuing high prices for oil and gas in 2003. Turkey's economy, however, registered a fairly sharp slowdown, primarily on account of negative growth in agriculture. Prospects for 2004 are for an easing of the collective growth rate of the subregion. India's agricultural sector is expected to slow somewhat after its impressive performance in 2003 and Turkey's economy is expected to come up against sluggish growth in the European Union, its principal trading partner.

15. Despite steady GDP growth over the last three years, this subregion is faced with a number of daunting challenges. For instance, income poverty levels remain high and access to essential social services, such as education and health, and to clean drinking water remains limited. The recent improvement on the macroeconomic front suggests that most, though not all, economies of the subregion have taken an important step in the right direction in improving the environment for investment decisions and hence for stronger long-term growth. At the same time, however, as GDP growth rates trend upward in the years ahead, the Governments of the subregion need to ensure that there is no slippage in the momentum. The emphasis on structural reform and improved governance, which has already provided a significant uplift to economic performance, must be maintained. In addition, Governments must ensure that the higher growth translates into more resources for the provision of social services and for infrastructure investments, two long-neglected areas of public policy over the years.

16. Despite the impact of SARS, collective GDP growth in South-East Asia in 2003 exceeded the pace achieved in 2002. Indonesia, Malaysia, Thailand and Viet Nam maintained their 2002 pace of rebound following the 2001 slowdown, while Cambodia, the Lao People's Democratic Republic, Myanmar, the Philippines and Singapore experienced reductions in their growth rates. The worst affected country was Singapore, where growth fell below 1 per cent in 2003. With the exception of the Lao People's Democratic Republic and Myanmar, where inflationary pressures remained high, the subdued pace of price increases slowed further in these economies. In virtually the entire subregion, GDP growth was stimulated by intraregional trade and domestic demand, both investment and consumption. The service sector was hit by SARS, but the adverse effects were confined to the second quarter of 2003 and were reversed in the second half of the year. Prospects for 2004 are positive, with GDP growth expected to pick up further momentum in all countries of the subregion. Inflationary pressures, however, are likely to increase modestly as higher raw material and commodity prices enter the production chain.

17. South-East Asian countries have been some of the best-performing economies in the ESCAP region for many years and have made good progress in reducing poverty in the process. The 1997 crisis and the 2001 downturn not only reduced growth and worsened the macroeconomic situation, but also undid much of the impressive progress made in poverty reduction in the 1980s and early 1990s. The policy issues facing the subregion consequently consist of regaining the pre-crisis momentum of growth and making up lost ground in the area of poverty reduction. However, this will involve the resolution of significant structural problems that came to light following the 1997 crisis and where much still remains to be done, notwithstanding considerable progress over the last six years. First and foremost is the need to speed up reform of the corporate and financial sectors and to deal conclusively with the issues of lingering corporate balance sheet weakness and impaired assets in the financial sector. Without progress in this area, a major upturn in corporate investment levels and technological upgrading is unlikely to take place on a durable basis.

18. The second major and interconnected issue is that of public finance. Governments have run up public debt to a high level in refinancing the financial sector and supporting the momentum of growth. There now needs to be a time-bound programme of fiscal consolidation together with a rebalancing of direct and indirect taxes and of expenditures to promote equity and enhance the provision of public and merit goods. Third, in a rapidly changing regional environment, and especially in view of the challenge posed by China's rapid growth, the subregion needs to direct resources towards enhancing competitiveness through skills upgrading and the development of more domestic technology.

19. In the developed countries of the region, 2003 saw a strong revival of growth in Japan, the world's second-largest economy, that for the first time in a decade bears the promise of durability. Australia and New Zealand continue to show dynamism so that there is a basis for all three economies to achieve output growth at, or near to, their long-term potential for a number of years. As Japan's economy is a major source of demand for the region's exports and a major provider of foreign direct investment for the region, these developments augur well for the future.

20. The key policy objective in 2004 for this group of countries is to sustain growth. In Japan, this requires decisive action on the domestic policy front to resolve long-standing problems in the banking sector, in the massive public debt and in the chronic deflationary pressures, which prevent a durable recovery of consumption expenditures in the economy. In Australia and New Zealand, the problems have to do with the maintenance of prudent macroeconomic aggregates in the near term, namely, containing the current account deficit, so that the pace of growth does not slacken in the coming years.

II. Policy issues and challenges

21. Even with the relatively buoyant growth that the region is currently enjoying, new policy issues and challenges are sure to arise. Some will emanate from adverse changes in the global environment, where national policies can only play an attenuating role. Others will arise that are more domestic in both origin and import; here, national policies can be more normative and directly address the issues that have arisen.

22. Some of the potential and problematic policy issues facing the region, such as the unwinding of global imbalances and the weakening of the dollar, are primarily international in character, but individual economies should nonetheless take appropriate action to shield themselves from their deleterious effects. Acting together in cooperation will be more effective than acting alone. Other potential and problematic policy issues, such as the appreciation of regional exchange rates, will require flexibility of response and alertness buttressed by stronger regional cooperation so that, should difficulties arise, corrective action can be taken in time.

23. Another area requiring policy attention is the possible emergence of asset bubbles in stock markets and in real estate and whether pre-emptive action is the right course to adopt given the level of uncertainty involved in how bubbles come about in the first place and the efficacy of traditional policy instruments in dealing with them, such as interest rate changes. In this context, the accumulation of large foreign exchange reserves, apart from raising the question of opportunity costs, given the low returns available on them, has also constrained somewhat the freedom of the authorities in the conduct of monetary policy by putting upward pressure on exchange rates. Yet others are regional issues, such as the incidence of avian influenza, where action has to be national, but without strong subregional and regional cooperation in containing the spread of the disease such action might be of little use. Finally, all Governments need to place short-term issues within their longer-term commitments, such as those made in accepting the Millennium Development Goals.

24. In the following paragraphs, the principal policy issues facing the region are discussed against this background. These issues have been discussed in previous issues of the *Survey*, but the passage of time often provides fresh insights and a better understanding of the underlying policy trade-offs.

25. The need for fiscal consolidation is becoming paramount. Last year it was stressed that Governments in the region should announce credible targets and supporting policies to stabilize public debt vis-à-vis GDP at a sustainable level. There is a need now perhaps for Governments to adopt more formally debt-to-GDP ratios and annual budgetary deficits as the European Union has done in its Stability and Growth Pact. If implemented with flexibility rather than mechanically, such targets could introduce a useful element of predictability in their public finances, thereby providing a more secure and informed basis for investment decisions in the economies concerned.

26. The consolidation of public debt should ideally be approached within a long-term programme of fiscal reform. All national tax systems in the region need to be defined by the aim to make them more equitable and efficient. One problematic element in the administration of national tax systems is the discretionary powers given to tax officials. These tend to dilute accountability, open up opportunities for corrupt practices and lower efficiency. There are no easy solutions to these problems, especially if they have existed for a long time. Nevertheless, the ongoing improvement of equity and efficiency in the area of public finance should be a long-term, focal objective. Corruption is a serious barrier to effective resource mobilization and allocation, and diverts resources away from activities that are vital for sustainable development. Even small incremental steps to reduce corruption will have a major cumulative impact on public resource generation and allocation. One

obvious route to greater accountability is transparency in the award of major public sector contracts.

27. Corporate and financial sector reform has made significant progress in the region as a whole. However, there is still a case for speeding up the pace of reform in most economies of the region, in particular in those countries that appear to be lagging in the implementation process. In this regard, the reform programme could perhaps be linked to initiatives for the development of financial markets in the region. As local bond markets grow in individual countries and new sources of finance for small and medium-size enterprises, such as venture capital, become increasingly available, it may be worthwhile simultaneously to facilitate regional or subregional linkages between these national markets. The development of regional or subregional markets will foster a broader investor base and reduce risk and uncertainty. Countries in the region should identify the impediments to the development of regional markets and seek to remove them. Information and communication technology offers a means of integrating national markets that was not available before.

28. The key to steady development in the medium term is maintaining and enhancing competitiveness, a process requiring a stable macroeconomic environment and a continuing programme of investment in infrastructure and in public goods. Investment in human resources development is a critically important element in this regard and, in this connection, the main challenges are to improve the quality of education at the primary and secondary levels, reduce dropout rates and enhance the performance of underachievers. Many countries in the region are not doing enough in this area and clearly risk falling behind in competitiveness. One of the Millennium Development Goals calls for the achievement of universal primary education by 2015. Merely fulfilling this quantitative target will not be enough; Governments should lay equal stress on the quality of primary education so that the number of children going on to secondary education goes up and all school-leavers acquire skills that will both enhance national competitiveness and provide them with good employment opportunities.

29. Small and medium-size enterprises in most of the region's economies are a major source of employment and output. However, financial market infrastructure is poorly developed to assist such enterprises in growing to an efficient size. The persistence of capital market imperfections makes it more difficult for small firms to access financing in order to upgrade or expand. There is also resistance on the part of owners to provide reliable balance sheet information in order to gain improved access to finance. Many small firms thus find it difficult to reach a minimum efficient size and are prone to financial difficulties, causing in consequence wasted or misallocated capital. Governments should reinvigorate existing programmes of training, technology transfer, information dissemination and the formation and deepening of clusters and networks to improve the performance of small and medium-size enterprises.

30. Governance remains an ongoing policy challenge virtually throughout the region. Despite good progress in establishing sound frameworks for improved private and public sector governance over the last decade or so, the quality of implementation remains uneven. Lack of access, or differential access, to administrative or legal redress when citizens are confronted by problems or are involved in contractual disputes lowers the overall efficiency of investment, makes

investors risk-averse and almost certainly reduces total factor productivity. Governments must take due cognizance of and correct the most obvious shortcomings, such as an unresponsive State bureaucracy and interminable delays in the legal process. Having the right laws is not enough; they must be seen to be effective in practice. Corporate malfeasance and corruption by public officials need to be tackled vigorously across the region.

III. Poverty reduction strategies: tackling the multidimensional nature of poverty

31. Poverty is a complex phenomenon, with its dimensions reaching much beyond income. The *Survey* examines trends in selected dimensions of poverty to ascertain the nature and extent of poverty in countries of the region and critically reviews national poverty reduction strategies and programmes, including those dealt with in Poverty Reduction Strategy Papers (PRSPs), to bring out commonalities, share experiences and draw lessons for designing more effective policies and programmes.

Dimensions and magnitudes of poverty

32. Poverty, being a multidimensional concept, is not easy to define. The *Survey* highlights four approaches to defining poverty: the monetary approach, the capabilities approach, the social exclusion approach and the participatory approach. The monetary approach defines a poverty line in monetary income sufficient to attain a minimal standard of living, while the capabilities approach focuses on the ability to lead a long life, function without chronic morbidity, be capable of reading, writing and performing numerical tasks and be able to move from place to place.

33. The social exclusion approach emphasizes relations among individuals. Social exclusion occurs when individuals or groups are unable to participate fully in the society in which they live. The participatory approach takes into account the views of poor people themselves. The people themselves decide what it means to be poor and that determines the magnitude of poverty. In cases where all the approaches identify broadly the same people as poor, any single approach can be used for measuring poverty. However, the empirical evidence shows that poverty rates in countries differ significantly according to the approach adopted. As a result, policy options can differ depending on the approach selected.

Trends in income poverty

34. Income poverty is the most serious problem facing many developing countries in the region. Despite the incidence of poverty in the region coming down from 37 per cent in 1990 to 25 per cent in 1999, based on the dollar a day poverty line, more than two thirds of the world's poor live in Asia and the Pacific.

35. The regional data mask the diverse performance of the countries. On the basis of the one dollar a day poverty line, poverty has been virtually eliminated in some countries, while many others continue to grapple with it (see table 2). Extra effort at both the national and regional levels would be necessary to enable those countries to make a dent in poverty reduction and achieve the Millennium Development Goals.

Table 2
Population below the one dollar poverty line in selected countries, 1990-2002
(Percentage)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Bangladesh	..	..	35.9	..	..	..	29.1	..	..	..	36.0	..	..
Cambodia	48.3	..	..	..	..	..	36.7	38.4	37.7	41.7	44.6	45.0	44.2
China	31.5	..	..	29.0	..	..	16.4	..	16.1	17.8	15.4	14.3	12.7
India	46.6	..	51.1	..	45.1	47.1	46.2	44.2	..	34.7	..	..	..
Indonesia	20.6	..	..	14.8	..	..	7.8	..	..	12.0	9.9	9.2	7.2
Kazakhstan	..	..	..	1.1	..	..	1.5	..	..	..	..	..	..
Kyrgyzstan	..	..	..	23.0	..	..	..	1.6	..	..	2.0	..	..
Lao People's Democratic Republic	53.0	..	48.8	..	..	..	41.3	38.4	36.6	36.7	35.1	31.3	30.0
Malaysia	2.0	..	1.5	..	..	1.0	0.8	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5
Mongolia	..	..	..	..	..	13.9	..	..	..	..	..	..	..
Nepal	..	..	..	..	..	37.7	..	..	..	..	..	..	..
Pakistan	47.8	..	..	33.9	..	..	31.0	..	..	..	..	..	..
Papua New Guinea	35.4	..	..	..	..	..	24.6	25.6	27.8	30.7	35.3	38.2	42.8
Philippines	19.1	19.8	..	..	18.4	..	14.8	12.1	13.7	13.5	13.5	11.9	11.5
Republic of Korea	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5	<0.5
Russian Federation	..	..	..	6.2	..	..	7.2	..	7.1	..	6.1	..	..
Sri Lanka	3.8	..	..	..	..	6.6	..	..	..	..	..	..	..
Thailand	12.5	..	6.0	..	..	..	2.2	..	3.3	3.1	5.2	3.6	2.4
Turkmenistan	..	..	..	20.1	..	..	..	..	12.1	..	..	..	..
Viet Nam	50.8	..	..	39.9	..	..	23.6	..	16.4	16.9	15.2	14.6	13.6

Sources: World Bank, *East Asia Update: Regional Overview*, October 2003, www.worldbank.org.cn/English/ Content/ EAP10-03.pdf, 20 November 2003, and global poverty monitoring web site, www.worldbank.org/ research/povmonitor, 17 June 2003.

National strategies for poverty reduction

36. Despite robust growth in the region as a whole, poverty continues to be a persistent problem in many countries. The success of East Asian economies up until the 1990s and China's achievements in making major inroads in poverty reduction in the 1990s confirm how high levels of growth can induce broad-based development and reduce poverty within a relatively short period. Macroeconomic stability, openness to international trade, human resources development and the rule of law underpinned high economic growth in those economies. Meanwhile, the Asian economic crisis in 1997 highlighted the necessity for institution-building to consolidate the aforementioned gains and avoid the pitfalls of liberalization.

37. In a number of countries, even when the economies are growing there has not been a commensurate improvement in the quality of life of the poorer sections of society. Poverty continues to persist because of inequitable distribution of the benefits of growth. The traditional approaches to development through national

planning and structural adjustment have had little impact on poverty reduction in many developing countries, as the central theme of such policies was not poverty reduction but growth and stability. Country experiences suggest that, in addition to sustained growth, measures designed specifically to increase access to economic opportunities for the poor are necessary if the benefits of growth are to be distributed evenly and poverty is to be eliminated on a sustainable basis.

38. PRSPs, whose core objectives are broad-based growth and poverty reduction, are a direct response to these issues. The PRSP approach is based on five core principles: it is country-driven, results-oriented, comprehensive and partnership-oriented and takes a long-term perspective for poverty reduction.

39. The *Survey* examined the poverty reduction strategies of 21 countries, including six interim PRSPs and seven full PRSPs. The overwhelming majority of those papers identify the lack of access to assets and basic needs, such as education, health care and safe drinking water, as the most critical issues concerning poverty and development. Several other country-specific issues, such as gender inequality, internal crisis and natural disaster, have also been highlighted as causes of poverty.

40. National strategies recognize the importance of both high-quality growth and pro-poor policies in reducing poverty on a sustainable basis. Reflecting this, the policy approach under PRSPs focuses on a combination of macroeconomic policies and structural reforms, such as financial sector reforms, fiscal reforms, trade liberalization, reforms in the agricultural sector and labour market reforms aimed at growth and stability, as under previous Structural Adjustment Facility and Enhanced Structural Adjustment Facility-related programmes, together with pro-poor policies particularly aimed at capacity-building for the poor.

41. The PRSP approach reflects a significant deviation from the previous adjustment processes by focusing on institutional developments that would be required for the effective implementation of such policies and the development of infrastructure, both urban and rural, to enhance a country's capacity for socio-economic development.

42. The inclusion of pro-poor policies, in particular policies for building the capacity of the poor and targeted social safety nets for the vulnerable, indicates a major shift in development policy advocated by multilateral lending agencies. Building the capacity of the poor is a key component of any sustainable poverty reduction strategy, as it would allow mainstreaming of the poor into the development process. PRSPs identify three major components of capacity-building: (a) empowerment; (b) providing opportunities; and (c) enhancing security.

43. The majority of the PRSPs have focused on empowering women as a development strategy, particularly in reducing the broader aspects of poverty. The underlying reasoning is the fact that in most developing countries gender gaps are widespread and the cost of ignoring such disparities is very high and increasing gender equity can have a positive effect on productivity and the human capital of the next generation.

44. The provision of social safety nets to vulnerable groups is an essential part of poverty reduction strategies, although it is not a substitute for policies to deal with social exclusion or the building up of capabilities. Fallouts from market-based policies, inequality in the distribution of assets and lack of opportunities could drive certain sections of society into poverty. In addition, the *Survey* finds that people in

developing countries in the Asia-Pacific region are driven into poverty by three other specific factors: increasing prevalence of diseases, particularly HIV/AIDS; inability to adjust to market economic systems; and social division and internal conflicts.

45. Recognizing the environment-poverty nexus, several countries have attempted to strike a balance between the existing livelihood requirements of the people and sound environmental resource management that can ensure sustainability by integrating environmental conservation into their national poverty alleviation strategies.

Handling the multidimensional aspects of poverty in PRSPs

46. Since poverty is a complex and multidimensional phenomenon, dealing with it requires a holistic approach that addresses cross-cutting development issues along with growth. However, dealing with various dimensions of poverty may require that priorities be set owing to financial and other resource constraints.

47. PRSPs are new and involve a learning process for many; there is therefore much room for improvement in country approaches to addressing cross-cutting issues aimed at reducing poverty on a broader scale. As such, achieving the Millennium Development Goals would greatly depend on the successful implementation of poverty reduction strategies built on a broader development framework. This is particularly important as PRSPs are to be used as the primary tool for achieving the Goals.

48. Although it is claimed that PRSPs are country-owned, external development partners continue to have a significant influence in policy formulation, effectively nullifying the country ownership. The pressure from external development partners would bias country strategies towards the agenda of multilateral lending agencies. In many instances, both bureaucratic and political ownership are lacking, while consultations with civil society have been limited. PRSPs could be made nationally-owned and acceptable to the communities at large by broadening the consultative process to involve civil society effectively and reflect its voice in the policy agenda.

49. PRSPs, which are linked to external financing, tend to be biased towards macroeconomic stability and growth rather than pro-poor policy strategies. The impact of macroeconomic stabilization policies on growth and poverty reduction needs to be assessed properly to ensure that the policies adopted are the most effective ones for reducing poverty on a sustainable basis. As the overarching objective of PRSPs is poverty reduction, more emphasis needs to be given to policies aimed at poverty reduction, while paying attention to macroeconomic stabilization to ensure sustainability.

50. The *Survey* finds that the relationship between PRSPs and the Millennium Development Goals is weak, as only a few PRSPs have benefited from any kind of analysis of the Goals in the preparation of poverty reduction strategies. The poverty reduction strategies in PRSPs or national development plans usually focus on a medium-term span of 3 to 5 years, while the Millennium Development Goals are set for 2015, a long-term target. Although several low-income countries have spelled out their own long-term visions even beyond 2015 and in certain cases linked them to the Millennium Development Goals, the link between such long-term goals and policy actions taken at present is very weak, with no underlying resource

commitment or policy approach, often leading to a vacuum in between. The PRSP targets could be directly linked to the Millennium Development Goals through intermediary targets set in PRSPs.

51. Country strategies reflected the lack of a proper poverty assessment, while some others did not focus their policy strategies on addressing the priority issues. The lack of technical and financial capacity appears to have constrained countries in developing an effective and comprehensive poverty reduction strategy. Some poverty reduction strategies do not provide an in-depth analysis of the root causes of poverty. Several others do not focus their policy on critical areas. For example, landlessness, unemployment and the gender gap, which have been identified as major causes of poverty, among other things, have not received adequate focus in the policy agenda for poverty reduction in certain instances.

52. The lack of a proper assessment of poverty makes poverty reduction strategies ineffective and the socio-economic outcomes of policy actions could deviate heavily from the desired goals. The medium-term policy matrices under PRSPs usually contain a long list of policy actions to be undertaken by Governments, reflecting the ambitiousness of the exercise. However, the pacing and prioritization of policy strategies need to be strengthened to ensure that policy strategies are implemented effectively, taking account of financial resource constraints as well as limitations in absorptive capacity. Policy strategies under PRSPs could be made effective if burning issues are addressed immediately.

53. The medium-term macroeconomic projections in PRSPs are often incomplete, overly optimistic and inadequately substantiated, and the analysis of the underlying economic and structural policies required for achieving such targets are weak, making policy outcomes less appealing. The reason for having overly optimistic macroeconomic projections, in particular the economic growth projections, could be due to their political sensitivity. Realistic targets are needed to keep the policy agenda on track and ensure that the ultimate objectives are met.

54. In several countries, little effort has been made to harmonize poverty reduction strategies and national plans owing to the lack of coordination between different branches of Government and the lack of clarity in their roles, the preparation of PRSPs and national development plans by separate agencies without close coordination and the lack of political acceptance. Such disparities could also emerge when multilateral lending agencies influence the PRSP preparatory process without taking account of national priorities and socio-economic conditions. This could lead to divergent policies and strategic directions. Harmonization of PRSPs and national development plans is essential to ensure that policy implementation by various agencies is consistent with country strategies for poverty reduction.

55. One of the major weaknesses of PRSPs is the lack of evaluation of downside risks of external and internal shocks, such as the deterioration of the terms of trade, recessionary conditions in industrial countries and the phasing out of the Multi-Fibre Arrangement for achieving the targets set for each year. Alternative contingency policy scenarios reconciling macroeconomic projections with these concerns and the trade-offs underpinning these choices are necessary if Governments are to minimize the deviation between actual performance and the original targets.

56. In many instances, macroeconomic frameworks emerging from PRSPs and those used for national budgeting processes are not closely linked, even when the

countries concerned are receiving programme support from multilateral lending agencies, such as the International Monetary Fund and the World Bank. In some PRSPs the medium-term expenditure framework is not well linked to the PRSP or the budget. Except for a few, Parliaments in the respective countries do not appear to have played a significant role in the PRSP process. This disconnection between policy frameworks under PRSPs and national development plans and the national budgets could nullify efforts to meet the Millennium Development Goals, as policy actions could deviate from the proposed policy agenda. Policy strategies alone are not sufficient to achieve goals; they must be followed by actions. Integrating the PRSP as an important input to government decision-making and budgetary processes is vital for the effective implementation of policies aimed at broad-based poverty reduction, as it enables policy design and costing of policy strategies to be matched with government priorities.

57. Effective monitoring and evaluation of the progress of poverty reduction strategies is essential for ensuring that the development targets are met. Such mechanisms also facilitate the identification and rectification of major institutional and resource constraints. The PRSP process being new, monitoring and evaluation would necessarily be an evolving process. Although some countries have proposed establishing separate units or teams for monitoring and evaluation, proper monitoring systems have yet to be developed.

58. Capacity constraints would constitute a major problem in effective monitoring and evaluation of poverty reduction strategies in many PRSP countries. This is one area where donor support could make a difference in scaling up capacity-building in monitoring and evaluation at the country level.

59. The international community, as a major stakeholder in global efforts to reduce poverty, can play a critical role in facilitating country efforts. The international community's direct involvement in the PRSP process would, in addition to providing financial and technical support, help to ensure Governments' commitments to undertake policy strategies needed to reduce poverty on a sustainable basis.

60. Addressing broad-based poverty issues at the global level would benefit not only low-income countries but also industrialized countries directly and indirectly, as emphasized in various global declarations, such as the Monterrey Consensus and the Johannesburg Plan of Implementation. While poverty reduction in low-income countries could create a larger market for industrial country goods and services, provide a source of inputs for their products, including knowledge and skills and expand opportunities for advanced country investments, it also addresses emerging social issues, such as global terrorism and the spread of diseases, which would benefit all. As such, the industrial countries and multilateral lending agencies could complement efforts by low-income countries to reduce poverty, in particular by:

(a) Providing technical assistance in capacity-building for the design of poverty reduction strategies under the PRSP process and for monitoring;

(b) Providing support for countries to undertake poverty and social impact analysis;

(c) Opening industrial country markets to developing country exports and phasing out trade-distorting subsidies;

(d) Helping to bridge the financial gap to meet the resource requirements for undertaking poverty-related development policies.

61. Such initiatives would facilitate the achievement of the goals of eradicating poverty and sustainable development as expressed in the Monterrey Consensus and also in developing a global partnership for development, as set out in Millennium Development Goal 8.

62. The fact that PRSPs are the primary strategic and implementation vehicles to achieve the Millennium Development Goals would essentially require the involvement of the United Nations in the PRSP process. This is particularly important owing to the multidimensional nature of poverty, in which the United Nations system has a niche, particularly in those areas which are not usually taken care of by stabilization policies alone. Fostering national ownership, capacity-building for the preparation, monitoring and evaluation of PRSPs, implementation of pro-poor policies and donor coordination (including the private sector) to fill the financing gap are some of the areas where the United Nations can be directly involved to make PRSPs more Millennium Development Goals-friendly and achieve the poverty reduction targets set for 2015.